

BEFORE
THE PUBLIC SERVICE COMMISSION OF
SOUTH CAROLINA
DOCKET NO. 94-739-S - ORDER NO. 95-1578 ✓
OCTOBER 3, 1995

IN RE: Application of Quail Hollow Utilities,) ORDER
Inc. for Approval of an Increase in) APPROVING
Sewer Rates and Charges.) RATES AND
) CHARGES

This matter comes before the Public Service Commission of South Carolina (the Commission) by way of an Application of Quail Hollow Utilities, Inc. (Quail Hollow or the Company) for approval of a new schedule of rates and charges for its customers in South Carolina. The Company's April 7, 1995 Application was filed pursuant to S.C. Code Ann. §58-5-240 (Supp. 1994), and R.103-821 of the Commission's Rules of Practice and Procedure.

By letter, the Commission's Executive Director instructed the Company to publish a prepared Notice of Filing, one time, in a newspaper of general circulation in the area affected by the Company's Application. The Notice of Filing indicated the nature of the Company's Application and advised all interested parties desiring participation in the scheduled proceeding of the manner and time in which to file the appropriate pleadings. The Company was likewise required to notify directly all customers affected by the proposed rates and charges. The Company filed affidavits, showing that it had complied with the instructions of the

Executive Director.

Petitions to Intervene were filed on behalf of the Consumer Advocate for the State of South Carolina (the Consumer Advocate), and the Quail Hollow Community Association, Inc. (the Association).

The Commission Staff made on-site investigations of the Company's facilities, audited the Company's books and records, and gathered other detailed information concerning the Company's operations.

A public hearing relative to the matters asserted in the Company's Application was held on August 24, 1995, in the Commission's offices at 111 Doctors Circle, Columbia, South Carolina. Pursuant to S.C. Code Ann. §58-3-95 (Supp. 1994), a panel of three Commissioners composed of Commissioners Scott, Bradley, and Arthur was designated to hear and rule on this matter. Commissioner Scott presided. William F. Austin, Esquire, and Richard L. Whitt, Esquire, represented the Applicant; Elliott F. Elam, Jr., Esquire, represented the Intervenor Consumer Advocate; J. Thomas Falls, Jr., Esquire, represented the Intervenor Quail Hollow Community Association, Inc., and F. David Butler, General Counsel, represented the Commission Staff.

The Company presented the direct testimony of Robert R. Russell, Jr., President of the Company, and Thomas D. Pietras, Certified Public Accountant. The Commission Staff presented the testimony of Maria Walker, Public Utilities Accountant, and William O. Richardson, Utilities Engineer Associate III.

Quail Hollow's present rates were approved by Commission Order No. 88-497, issued May 23, 1988 in Docket No. 87-265-S for Quail Hollow Company General Partnership. At that time, the residential monthly charge per single residence or single family equivalent (SFE) of \$17.00 was approved by the Commission. Effective May 4, 1994, all assets, liabilities, equity and operations of the sewer system were transferred from the partnership to Quail Hollow. The Applicant now requests a residential monthly charge per residence or SFE of \$25.00 which includes a charge of \$1.15 per 1,000 gpd by the City of West Columbia.

The Company provides sewer service to 570 customers, including 215 apartments units in the Quail Hollow Subdivision, Lexington County, South Carolina. According to Staff testimony, the sewer system consists of mains, two lift stations, a flow meter, and housing. The City of West Columbia collects and treats the sewage from the subdivision for Quail Hollow.

After a consideration of the entire record in this case, including the testimony and all the exhibits, the Commission makes the following findings of fact.

FINDINGS OF FACT

1. The Company is a sewer utility operating in the County of Lexington, State of South Carolina and is subject to the jurisdiction of the Commission pursuant to S.C. Code Ann. §58-5-10 et seq. (Supp. 1994).

2. The Company provides sewer service to approximately

570 residential customers, including 215 apartment units in Quail Hollow Subdivision, Lexington County, South Carolina.

3. Quail Hollow's present rates and charges were approved by Commission Order No. 88-497, issued May 23, 1988 in Docket No. 87-265-S, for Quail Hollow Company General Partnership. At that time, the Commission approved a rate of \$17.00 for residential monthly charge per residence or SFE.

4. At present, the Company charges a flat rate of \$17.00 per single residence or SFE. The Company is seeking an increase of this amount to a \$25.00 monthly charge per single residence or SFE, this includes a charge of \$1.15 per 1,000 gpd by the City of West Columbia.

5. The Company asserts that this requested rate increase is required because the Company's expenses have increased across the board.

Robert R. Russell, Managing Agent testified that he has made numerous attempts to deed the sewer system to the homeowners, and to the City of West Columbia. At present, the expenses incurred for the period ending May 31, 1995 have increased. According to Russell, the expenses far exceed the Company's revenues. Russell states his belief that a rate of \$25.00 per month is fair and reasonable, although he is willing to discuss deeding the system to any party that will operate the sewer system.

The Company has experienced for the test year, after accounting and pro forma adjustments, a loss of \$20,437. The operating margin, after interest expense, under current rates,

after accounting and pro forma adjustments was (17.22%).

6. The Company proposes that the appropriate test period to consider its requested increase is the twelve (12) month period ending May 31, 1995. The Staff concurred in using the same test year for its accounting and pro forma adjustments.

7. Under its presently approved rates, the Company's operating margin, after interest and after accounting and pro forma adjustments is (17.22%). The Company seeks an increase in its rates and charges for sewer service which would result in an operating margin of 14.46%.

8. Under the Company's presently approved rates, the Company's operating revenues for the test year, after accounting and pro forma adjustments are \$118,680. The Company seeks an increase in its rates and charges for sewer service in a manner which would increase its operating revenues by \$54,720 to a total of \$171,000.

9. The Staff asserts that under its presently approved rates, its total operating expenses for the test year, after accounting and pro forma adjustments are \$139,117.

The Commission has examined the accounting adjustments proposed by the Staff and the Company in this proceeding, and adopt Staff's adjustments with two exceptions. First, Staff has excluded \$2,400 in rental income from the Company's revenue. We disagree with this approach, and hold that the Company is entitled to claim the \$2,400 rental income. Further, we believe that the City of West Columbia litigation fees in this case should be

eliminated, contrary to the Staff's position, in that we believe these should be considered as below the line as not benefiting the ratepayers.

10. The Staff calculated the Company's net operating income after accounting and pro forma adjustments to be (\$20,437), and its net income for return to be (\$20,437).

11. The Company has applied for rates which will result in a operating margin after interest to be 14.46% under the proposed rates in assuming Staff's adjustments.

CONCLUSIONS OF LAW

1. The Company is a sewer utility providing sewer service in its service area in South Carolina. The Company's operations in South Carolina are subject to the jurisdiction of the Commission pursuant to S.C. Code Ann. §58-5-10 et seq. (Supp. 1994).

2. A fundamental principle of the ratemaking process is the establishment of an historical test year with the basis for calculating a utility's rate base and, consequently, the validity of the utility's requested rate increase. While the Commission considers a utility's proposed rate increase based upon occurrences within the test year, the Commission will also consider adjustments for any known and measurable out-of-test year changes in expense, revenues, and investments, and will also consider adjustments for any unusual situations which occurred in the test year. See, Parker v. South Carolina Public Service Commission, 280 S.C. 310, 313 S.E.2d 290 (1984), citing City of

Pittsburgh v. Pennsylvania Public Utility Commission, 187 P.A. Super. 341, 144 A.2d 648 (1958); Southern Bell v. The Public Service Commission, 270 S.C. 590, 244 S.E.2d 278 (1978).

3. The Company chose the test year ending May 31, 1995. The Commission Staff used the same test year in calculating its adjustments. The Commission is of the opinion that the test year ending May 31, 1995, is appropriate for the purposes of this rate request based on the information available to the Commission.

4. The Commission concludes that the Staff's adjustments to the Company's operating revenues are appropriate for the purposes of this Order with one exception. The Commission believes that the \$2,400 in rental income should be allowed to the Company. Other than that, the Staff's adjustments recognize an appropriate level of revenue for the Company for the test year under the present rates, and after accounting and pro forma adjustments to be \$146,040.

5. The Commission also concludes that the Staff's adjustments to the Company's operating expenses are appropriate for the purposes of this Order with one exception, that being \$3,364 for West Columbia litigation expenses. We do not believe these benefited the ratepayers.

6. Accordingly, the Commission concludes that the Company's appropriate operating expenses for the test year, after pro forma and accounting adjustments is \$140,687.

7. The Company's appropriate total income for return for the test year, after accounting and pro forma adjustments is

\$5,353. Based upon the above determinations concerning the accounting and pro forma adjustments, the Company's revenues and expenses, the Commission concludes that the total income for return is as follows:

TABLE A
TOTAL INCOME FOR RETURN

Operating Revenues	\$118,680
Operating Expenses	139,117
Net Operating Loss	(\$20,437)
Customer Growth	-0-
Total Income for Return	<u>(\$20,437)</u>

8. Under the guidelines established in the decisions of Bluefield Water Works and Improvement Co. v. Public Service Commission of West Virginia, 262 U.S. 679 (1923), and Federal Power Commission v. Hope Natural Gas Co., 320 U.S. 591 (1944), this Commission does not ensure through regulation that a utility will produce net revenues. As the United States Supreme Court noted in Hope, a utility "has no constitutional rights to profits such as are realized or anticipated in highly profitable enterprises or speculative ventures." However, employing fair and enlightened judgment and giving consideration to all relevant facts, the Commission should establish rates which will produce revenues "sufficient to assure confidence in the financial soundness of the utility and... that are adequate under efficient and economical management, to maintain and support its credit and enable it to raise the money necessary for the proper discharge of its public duties." Bluefield, supra, at 692-693.

9. There is no statutory authority prescribing the method which this Commission must utilize to determine the lawfulness of the rates of a public utility. For a sewer utility whose rate base has been substantially reduced by customer donations, tap fees, contributions in aid of construction, and book value in excess of investment, the Commission may decide to use the "operating ratio" and/or "operating margin" method for determining just and reasonable rates. The operating ratio is the percentage obtained by dividing total operating expenses by operating revenues; the operating margin is determined by dividing the net operating income for return by the total operating revenues of the utility. This method was recognized as an acceptable guide for ratemaking purposes in Patton v. South Carolina Public Service Commission, 280 S.C. 288, 312 S.E.2d 257 (1984).

Based on the Company's gross revenues for the test year, after accounting and pro forma adjustments under the presently approved schedules, the Company's operating expenses for the test year after accounting and pro forma adjustments, and customer growth, the Company's present operating margin is as follows:

TABLE B
OPERATING MARGIN

BEFORE RATE INCREASE

Operating Revenues	\$118,680
Operating Expenses	139,117
Net Operating Income	<u>\$(20,437)</u>
Customer Growth	-0-
Total Income for Return	<u>\$(20,437)</u>
Operating Margin (After Interest Expense)	<u>(17.22%)</u>

10. The Commission is mindful of the standards delineated in the Bluefield decision and of the need to balance the respective interests of the Company and of the consumer. It is incumbent upon this Commission to consider not only the revenue requirements of the Company but also the proposed price for the sewer service, the quality of the sewer service, and the effect of the proposed rates upon the consumer. See, Seabrook Island Property Owners Association v. S.C. Public Service Commission, Op. No. 23351 (Filed Feb. 25, 1991); S.C. Code Ann. §58-5-290 (1976), as amended.

11. The three fundamental criteria of a sound rate structure have been characterized as follows:

... (a) the revenue-requirement or financial-need objective, which takes the form of a fair-return standard with respect to private utility companies; (b) the fair-cost apportionment objective which invokes the principle that the burden of meeting total revenue requirements must be distributed fairly among the beneficiaries of the service; and (c) the optimum-use or consumer rationing under which the rates are designed to discourage the wasteful use of public utility services while promoting all use that is

economically justified in view of the relationships between costs incurred and benefits received.

Bonbright, Principles of Public Utility Rates (1961), p. 292.

12. Based on the considerations enunciated in Bluefield and Seabrook Island on the fundamental criteria of a sound rate structure as stated in Principles of Public Utility Rates, and on the Stipulation between the Company and the Consumer Advocate, the Commission determines that the Company should have the opportunity to earn a 3.67% operating margin. In order to have a reasonable opportunity to earn a 3.67% operating margin, the Company will need to produce \$146,040 in annual operating revenues.

**TABLE C
OPERATING MARGIN**

AFTER RATE INCREASE

Operating Revenues	\$146,040
Operating Expenses	<u>140,687</u>
Net Operating Income	5,353
Customer Growth	-0-
Total Income for Return	<u>\$ 5,353</u>
Operating Margin (After Interest Expense)	<u>3.67%</u>

13. In fashioning rates to give the Company the required amount of operating revenues so that it will have the opportunity to achieve a 3.67% operating margin, the Commission has carefully considered the concerns of the Company's customers, and the concerns of the Quail Hollow Property Owners Association. The Company is encouraged to continue to improve the quality of the service it provides its customers. The Commission recognizes that

the proposed increase for sewer customers amounts to a four dollar increase in the average customer's bill. The rates designed herein consider the quality of the service provided by the Company to its customers and the need for the continuance of the provision of adequate service, as well as the impact of the increase on those customers receiving service and the Stipulation between the Company and the Consumer Advocate.

14. The Commission recognizes the increase in operating expenses and the additional expenses felt by the Company. The Commission further recognizes that under the current rates, the Company is experiencing a low operating margin.

15. The Commission concludes that an increase in rates is necessary, and that the proposed increase is unjust and unreasonable, however, the Commission believes that an increase from \$17.00 to \$21.00 per month is just and reasonable.

16. Based on the above considerations and reasoning, the Commission hereby approves the rates and charges as stated in this Order and attached hereto as Appendix A as being just and reasonable. The rates and charges approved are designed in such a manner in which to produce and distribute the necessary revenues to provide the Company the opportunity to earn the approved operating margin.

17. Accordingly, it is ordered that the rates and charges attached on Appendix A are approved for service rendered on or after October 1, 1995. The rate schedule is hereby deemed to be filed with the Commission pursuant to S.C. Code Ann. §58-5-240

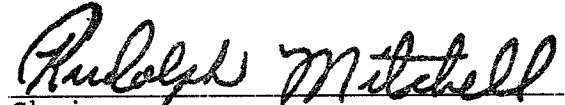
(Supp. 1994), as amended.

18. It is ordered that should the approved schedule not be placed into effect before three (3) months after the effective date of this Order, then the approved schedule shall not be charged without written permission of the Commission.


19. It is further ordered that the Company maintain its books and records for sewer operations in accordance with the NARUC Uniform System of Accounts for Class A and B utilities, as adopted by this Commission.

20. This Order shall remain in full force and effect until further Order of the Commission.

BY ORDER OF THE COMMISSION:


Chairman

ATTEST:


Deputy Executive Director

(SEAL)

APPENDIX A

QUAIL HOLLOW UTILITIES, INC.
1022 CALHOUN STREET
COLUMBIA, SC 29201
(803) 779-6000

FILED PURSUANT TO:

DOCKET NO. 94-739-S

ORDER NO. 95-1578

DATED: OCTOBER 3, 1995

RATES EFFECTIVE: OCTOBER 1, 1995

SEWER SERVICE

RESIDENTIAL - monthly charges per single
residence or single family
equivalent -----\$21.00